

VZCZCXRO7384
RR RUEHLMC
DE RUEHUM #0227/01 1400920
ZNR UUUUU ZZH
R 190920Z MAY 08
FM AMEMBASSY ULAANBAATAR
TO RUEHC/SECSTATE WASHDC 2169
INFO RUEHBJ/AMEMBASSY BEIJING 6166
RUEHUL/AMEMBASSY SEOUL 3366
RUEHKO/AMEMBASSY TOKYO 3041
RUEHMO/AMEMBASSY MOSCOW 2258
RUEHOT/AMEMBASSY OTTAWA 0628
RUEHBY/AMEMBASSY CANBERRA 0286
RHEHAAA/NSC WASHINGTON DC
RUEHLMC/MILLENNIUM CHALLENGE CORP WASHINGTON DC
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDO/DEPT OF COMMERCE WASHINGTON DC
RUEHC/DEPT OF INTERIOR WASHINGTON DC
RUEKJCS/SECDEF WASHINGTON DC

UNCLAS SECTION 01 OF 03 ULAANBAATAR 000227

SENSITIVE
SIPDIS

STATE PASS USTR, USTDA, OPIC, USGS, AND EXIMBANK
STATE PASS DOI/BLM FOR TESS BENNINGTON
STATE FOR EAP/CM AND EB/IFD/OIA
USDOC FOR ITA
INTERIOR FOR BLM

E.O. 12958: N/A

TAGS: [EMIN](#) [EINV](#) [PREL](#) [ECON](#) [EFIN](#) [PGOV](#) [MG](#)

SUBJECT: EMBASSY SUPPORTS PEABODY IN MEETINGS WITH PRESIDENT, PM;
REVIEWS MINING CONCERNS

SENSITIVE BUT UNCLASSIFIED - NOT FOR INTERNET DISTRIBUTION.

11. (SBU) SUMMARY: Visiting Peabody Energy President for Northeast Asia, accompanied by the Charge and Peabody reps, met separately with Prime Minister Bayar on May 8 and President Enkhbayar on May 9. They underscored Peabody's continued interest in doing business in Mongolia and delivered draft recommendations for a framework for the development of Mongolia's coal industry, which President Enkhbayar had requested during his October 2007 visit to the U.S. PM Bayar was seized with addressing differences between MPs regarding two mining amendments - one that proposes a 51% government equity share in strategic deposits, and another that envisions a production sharing contract (PSC). Bayar considered the former too problematic and the latter more workable and politically tolerable. (Note: Parliament's regular session closed Friday, May 15, with no action on either amendment, though the MPs may yet return to discussions before campaigning begins officially at month's end for June 29 national parliamentary elections. End Note.) Bayar concluded that Mongolians share a common desire to develop mining, but lack a consensus on how to do so. President Enkhbayar noted Mongolians' only experience with mining was with the 100%-government-owned Erdenet copper mine, a joint venture with the Soviets/Russians. He explored various permutations of the 51% idea: 51% government equity, 51% of the profits, and at some future point, owning a controlling interest of 51% of the physical property to ensure Mongolia's sovereignty over its own territory. Enkhbayar suggested deposits might be distinguished by the sources of exploration funding between those discovered by government-funded exploration, such as the Tavan Tolgoi coal deposit, versus those found privately, such as the Oyu Tolgoi copper/gold deposit discovered by Ivanhoe, a Canadian mining firm (and now partnered with Rio Tinto). At both meetings, the Charge supported Peabody's efforts and reviewed concerns voiced by American mining firms. END SUMMARY.

PEABODY REPS VISIT

12. (SBU) A visiting Peabody Energy delegation led by Peabody's President for Northeast Asia, Mr. Tahir Tayeb, accompanied by the Charge and Peabody reps, held separate meetings with Prime Minister Bayar on May 8 and President Enkhbayar on May 9. The purpose of their visit was to underscore Peabody's continued interest in doing

business in Mongolia, and to deliver a study, requested by the President, providing recommendations for a framework for the development of the Mongolian coal industry.

USG SUPPORTS PEABODY; AMENDMENT CONCERNS NOTED

13. (SBU) In both meetings following Peabody's presentations, the Charge intervened to stress that the USG supports Peabody as a world leader in coal development with cutting-edge technology, noting that Peabody has been a exemplary model of high standards for local community support and environmental protection. The Charge said U.S. firms speak for themselves as to the specifics of given proposals, but that many firms had advised the USG that the proposed amendment requiring an unfunded 51% government equity share would make mining commercially unviable. The Charge also noted that the uncompensated "taking" of such a government share in an existing investment could trigger U.S. anti-expropriation laws and provisions under the existing US-Mongolian Bilateral Investment Treaty (BIT). Of the mining amendment proposals currently on the table, the production sharing contract seemed to have the flexibility needed by investors while also meeting Mongolia's sovereignty and domestic political needs - that the contract contained no new "redline deal-breakers." (Note: After each meeting, Peabody reps expressed appreciation for accompanying them and supporting Peabody, as well as for delivering these important points. End Note.)

PM: MONGOLIANS SHARE A COMMON DESIRE TO
DEVELOP MINING BUT NO CONSENSUS ON HOW TO DO IT

ULAANBAATA 00000227 002 OF 003

14. (SBU) During a cordial 70-minute meeting, PM Bayar thanked Tayeb for the framework document and noted that the Mongolian public shared a common desire to develop its mineral resources, but lacked a consensus on how to do so. At the moment, two proposals were before the Parliament, one enshrining a 51% government equity share in any strategic mineral development, and the second proposing a "production sharing contract" (PSC). He thought the former was essentially unpassable, given differences between the ruling Mongolian People's Revolutionary Party (MPRP) and the opposition Democratic Party (DP), while the latter might still provide sufficient flexibility to meet Mongolian interests and those of potential mining investors. He thought passage of either would be difficult, given the lack of clarity on the issues and because there was little time before Parliament would recess so MPs could focus on the June 29 Parliamentary elections.

PRESIDENT AMPLIFIES VIEWS ON MINING

15. (SBU) During a May 9 meeting that lasted nearly 90 minutes, President Enkhbayar reviewed the evolution of Mongolian thinking on government participation. Enkhbayar noted that Mongolia's mining experience was dominated by its 70-year relationship with the Soviet Union, during which state ownership was 100%, and Mongolia's only real experience stemmed from the joint ownership with Russia of the Erdenet copper mine. Mongolians did not understand the distinction between 100% national ownership of the mineral resources in the ground and less than that in the mining investment, development, and production process. He opined that MPs, who visited major U.S. mines in Wyoming and Utah in 2007, drew the wrong conclusions, equating 100% USG ownership of underground mineral resources with equity participation in development, which is not the case. (Note: These MPs have willfully misrepresented what they heard while reviewing Peabody's Powder River Basin coal operations in Wyoming. They subsequently informed the Mongolian public that the USG owned and operated coal mines. Rather, the USG owns the minerals in the ground, but does not operate any mines. Specifically, they were told that the USG owns the minerals in the ground (which is the same world over), that they license extraction of these minerals to private operations in which the USG had no ownership, financial or managerial role. The MPs, for unknown reasons, did not convey this truth to their colleagues or the Mongolian public, claiming instead that the USG owned and operated coal mines. End Note.) The

President also offered a lengthy explanation of the history of the concept of royalties.

51% GOVERNMENT SHARE CONFUSION

16. (SBU) Over the course of the conversation, Enkhbayar indicated that he supported a 51% government equity share in strategic deposits, but then shifted to say he meant 51% of the profits, and later stressed the importance of Mongolia ending up at some future point owning a controlling interest of 51% of the property, so that it was ultimately assured of sovereignty over its own territory. Tayeb replied that there were many other options available to ensure Mongolia's sovereign control, citing as an example the USG's controls exercised through its regulatory authority. Enkhbayar also mentioned the possibility of "right of first refusal" provisions or "golden shares" as other options. Enkhbayar stressed that Mongolia needed a stable, predictable regime if it hoped to attract needed investment to make mining possible. He was concerned that the PSC would each require separate negotiations, opening up the process to more government and parliamentary meddling. (Comment: Post believes this waffling on 51% reflects Enkhbayar's early support for the ill-defined and problematic concept. Exactly what he was referring to was never articulated -- whether that meant the mine's physical plant or the corporate entity conducting the operation or something else, a confusion commonly shared among most GOM interlocutors and the Mongolian public in general. Enkhbayar has yet to find a suitable formula for distancing himself from his earlier pronouncements and has taken to castigating the PSC, perhaps in part because it is the preferred political solution of the Prime

ULAANBAATA 00000227 003 OF 003

Minister, a political rival of the President. End Comment.)

WHO FUNDS EXPLORATION?

17. (SBU) The President suggested that another approach to answering the question would be to distinguish between those resources discovered by government-funded exploration, such as the Tavan Tolgoi coal deposit, versus that found through private investment, ala the Oyu Tolgoi copper/gold deposit discovered by Ivanhoe, a Canadian mining firm (and now partnered with Rio Tinto). (Comment: In Post's view, this is a spurious argument for several reasons. First, earlier exploration may have been government-funded, but the government did not act, usually using the services of Soviet/Russian geologists to conduct exploration. When the GOM issued exploration and mining licenses, it issued the licenses with no mention of future share/ownership rights for GOM on these properties. However, the exploration firms were and are required to reimburse the GOM for its exploration expenses, the precise calculation of which remains problematic, as in many cases the exploration was conducted between 20 and 50 years ago. As many companies have reimbursed the GOM for its past expenses, they often wonder how the GOM can make a claim on deposit based on past expenses for which it has been compensated. Furthermore, much of the exploration was done by the Soviets using outdated technology, and firms say they had to do much of it again themselves to verify reliability. End Comment.) Enkhbayar expressed confusion about the Powder River Basin approach in which an exploration firm, which invested its own funds, also had to participate in a tender, and was not assured of the recovery of its exploration costs.

19. (SBU) The President asked for further information and examples of how the transfer of ownership of mineral rights was handled in the U.S. and elsewhere. He said he was interested in "power-sharing" issues and processes. (Note: Mongolian experts and officials in the Ministry of Industry and Trade have suggested that we conduct a series of DVC's among our Bureau of Land Management, Parliament MPs, and senior Mongolian officials, such as President Enkhbayar, to clarify our U.S. practices. BLM has already held several events with Mongolian counterparts, providing information at the mid- to department-chief level. However, our colleagues at MIT have reported that senior officials and parliamentary decision makers doubt what their advisors are telling them because it varies with what the traveling MPs have said; and although they doubt the MPs,

senior Mongolian officials and MPs feel the need to hear what the U.S. does directly from the BLM source. End Note.)

GOLDBECK